CLEARY GOTTLIEB

Securities law and shareholder activism

June 9, 2022

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Introduction - Navigating the securities law landscape

Landscape overview and relevance

Law of April 1, 2007 and Royal Decree of April 27, 2007 on takeover bids

— The Takeover Bid Rules require (a) person(s) to launch a mandatory takeover bid in certain circumstances

? Can wolfpacks inadvertently satisfy the various requirements and become obligated to launch an MTO?

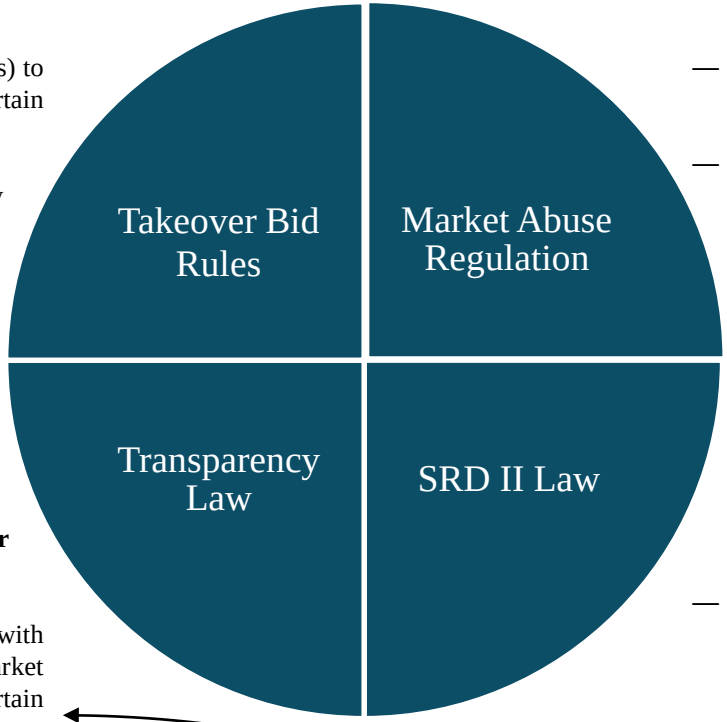
Regulation (EU) No 596/2014 of April 16, 2014 on market abuse

— MAR prohibits unlawful disclosure of inside information, insider dealing and market manipulation

— MAR also prescribes how investment recommendations can be disseminated

? Can activists engage in self-insider dealing?

? Are "short-and-distort" campaigns legal?



Law of May 2, 2007 and Royal Decree of February 14, 2008 on the disclosure of major shareholdings

— The Transparency Law requires investors with major shareholdings to disclose to the market the reaching, exceeding or falling below certain reporting thresholds

? Can activists covertly build up their stake?

? Do activists need to disclose their objectives when they acquire a major shareholding?

Law of April 16, 2020 transposing the Shareholder Rights Directive II

— The SRD II Law grants issuers the right to "look through" chains of intermediaries and identify their shareholders

? Can an activist make use of this right to rally support?

Zoom in on wolfpacks

What?

— Multiple activists congregating around a target, with one acting as a "lead" activist and others as peripheral activists

— Various forms of wolfpacks: loosely associated activists agitating the company with the same demands vs. well organized group with joint media campaign

— Can the company be a member of the "pack" in case there are opposing packs?

Issue?

— MAR limits in various ways the possibility for these activists to work together (*i.e.*, concerns around sharing of inside information and insider trading)

— Depending on the way a wolfpack is structured, the participating activists could be considered as "acting in concert" for purposes of the Transparency Law and Takeover Bid Rules

— Creates additional costs to engage in activist intervention due to the legal uncertainty arising out of the application of MAR and the acting in concert rules to collective shareholder actions

— For those considering commencing an activist intervention it is considered a significant legal risk

— Reason why – historically – there has been less activism in Europe?

Transparency Law and SRD II

Context

TRANSPARENCY DIRECTIVE

- Directive 2004/109/EC on the harmonization of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market
- Investors with major shareholdings must disclose to the market the reaching, exceeding or falling below certain reporting thresholds
- Each MS has adopted specific disclosure rules aimed at improving the transparency of relevant equity stakes and derivative instruments held in listed companies. Certain countries allow listed companies to adopt by-laws provisions, which require investors to notify the issuer when they hold significant stakes

Determines the size of the stake that activists can build up before being required to disclose their ownership

SHAREHOLDER RIGHTS DIRECTIVE II

- Directive (EU) 2017/828 amending Directive 2007/36/EC as regards the encouragement of long-term shareholder engagement
- Each MS has adopted rules allowing issuers to identify their shareholders. Option for MS to exclude from identification shareholders holding no more than 0.5% of an issuer's share capital

Allows issuers to proactively monitor stake-building by activist investors, including below notification thresholds

Both Directives have been implemented in Belgium through the Law of May 2, 2007 on the disclosure of major shareholdings in issuers whose shares are admitted to trading on a regulated market, as amended ("Transparency Law")

Disclosure of major shareholdings – Principles

No requirement to disclose intent

1 Notification trigger	— Any person who, directly or indirectly, acquires, transfers or holds voting securities, financial instruments equivalent to voting securities or voting rights of an issuer, which reach or cross (upwards or downwards) 5%, 10% or any subsequent multiple of 5% of the total voting rights, is required to submit a transparency notification with the issuer and the FSMA — Issuers may adopt the following additional notification thresholds in their articles of association: 1%, 2%, 3%, 4% and 7.5% (most issuers have adopted the 3% threshold) — Total outstanding voting rights (denominator) can be found on a dedicated section of the issuer's or the FSMA's website, in Form TR-1 BE and in the issuer's articles of association (which may be outdated) — A temporary crossing of a notification threshold (for a maximum of three Euronext trading days) is not notifiable
2 Notification format	— Notification to the issuer and the FSMA at the latest within four Euronext trading days following the triggering event — Standardized and automated Form TR-1 BE to be used (available on the website of the FSMA) — Notification may be in English, French or Dutch — Notifications are publicly disclosed by way of press release published on the issuer's website, and afterwards, on the FSMA's website
3 Sanctions?	— If a person failed to submit a transparency declaration at the latest 20 days prior to the relevant shareholders' meeting, such person cannot participate in the shareholders' meeting with respect to the relevant voting rights — If the notification has not been made in accordance with the modalities and within the time limits prescribed, the President of the competent Enterprise Court, acting as in summary proceedings, may (i) suspend the exercise of all or part of the rights attached to the related securities for a period of maximum one year, (ii) suspend a general meeting that has already been convened, or (iii) order the sale of the relevant securities to a third party

See also FSMA practical guide on the transparency rules

Disclosure of major shareholdings – "Equivalent" financial instruments

Article 6, §6 of the Transparency Law

[…] are equivalent to voting securities:

1° financial instruments that, on maturity, give the holder, under a formal agreement, either the unconditional right to acquire or the discretion as to his right to acquire, shares to which voting rights are attached, already issued, of an issuer whose shares are admitted to trading on a regulated market;

2° financial instruments which are not included in point 1° but which are referenced to shares referred to in that point and with economic effect similar to that of the financial instruments referred to in that point, whether or not they confer a right to a physical settlement.

For the purposes of the first paragraph, the following financial instruments shall be considered equivalent financial instruments provided they meet the conditions referred to in the first paragraph, 1° or 2°:

(a) transferable securities;

(b) options;

(c) futures;

(d) swaps;

(e) forward rate agreements;

(f) contracts for differences; and

(g) any other contracts or agreements with similar economic effects which may be settled physically or in cash.

This equivalence shall also apply to certificates not admitted to trading on a regulated market relating to voting securities if they give the holder the unconditional right or decision on that right to acquire the, already issued, voting securities to which they relate.

If the holder's right to acquire the underlying voting securities depends only on an event that the holder is able to trigger or prevent, such right shall be regarded as unconditional.

ESMA

"Indicative List of financial instruments that are subject to notification requirements according to Article 13(1b) of the revised Transparency Directive"

Also the following instruments are considered "equivalent instruments", provided they satisfy the criteria set out under 1° or 2°: "*(a) irrevocable convertible and exchangeable bonds referring to already issued shares, (b) financial instruments referenced to a basket of shares or an index, (c) warrants, (d) repurchase agreements, (e) rights to recall lent shares, (f) contractual buying pre-emption rights, (g) other conditional contracts or agreements than options and futures, (h) hybrid financial instruments, (i) combinations of financial instruments, and (j) shareholders' agreements having financial instruments as an underlying".*

Disclosure of major shareholdings – Example

(A) Voting rights	Previous notification	After the transaction			
	# voting rights	# voting rights		% of voting rights	
		Linked to securities	Not linked to securities	Linked to securities	Not linked to securities
	0	0		0.00%	
	0	0		0.00%	
	0	0		0.00%	
	0	0		0.00%	
	0	0		0.00%	
	4,157,385	1,757,385		2.13%	
Total	**4,157,385**	**1,757,385**	**0**	**2.13%**	**0.00%**

(B) Equivalent financial instruments	After the transaction					
	Type of financial instrument	Expiration date	Exercise period or date	# of voting rights that may be acquired if the instrument is exercised	% of voting rights	Settlement
	Equity Swaps	31/07/2020	N/A	2,400,000	2.91%	cash
	Equity Swaps	30/11/2020	N/A	3,709,074	4.50%	cash
	Equity Swaps	10/03/2029	N/A	2,453,407	2.98%	cash
TOTAL				**8,562,481**	**10.40%**	

	# voting rights	% of voting rights
TOTAL (A + B)	**10,319,866**	**12.53%**

1,757,385 voting securities

→ Give the shareholder **2.13% of the aggregate voting rights** in the issuer

This shareholder holds

8,562,481 financial instruments equivalent to voting securities

→ Give the shareholder an **economic exposure** similar to holding voting securities in the company representing 10.40% of the aggregate voting rights in the company

→ Do **not** give the shareholder any **voting rights** in the company…

- These equity swaps are settled in cash only, and therefore do not entail the physical delivery of any shares
- Contractual terms of the equity swaps do not grant the shareholder the right to acquire or otherwise obtain any voting securities

→ … **unless** the shareholder would itself acquire the voting securities underlying the equity swaps in a transaction that is distinct from the equity swaps

Right to identify shareholders

Limited to "shareholders"

Principles

— Listed companies have the right to "look through" the chain of intermediaries, and identify their shareholders, by directing a request for identification to the relevant intermediary

— Intermediaries include investment firms, credit institutions and central securities depositories (CSDs)

— Applies to all intermediaries as soon as they provide services to shareholders or other intermediaries related to shares of a listed issuer that has its statutory seat in Belgium, regardless of where that intermediary is based

— No threshold

Information

— The intermediary should communicate the following information to the company without delay:

- the shareholder's name and contact details;
- the number of shares held; and
- if so requested by the company, the classes of shares held and the acquisition date

GDPR

— The personal data of shareholders shall be processed in order to enable the company to identify its existing shareholders. The purpose is to communicate with them directly with the view to facilitating the exercise of shareholder rights and shareholder engagement with the company

In practice

— Facilitates **shareholder identification surveys** (by proxy tender solicitors / information agencies, as the case may be) by ensuring cooperation by the intermediaries

— Intermediaries should make public **fees** applicable for the provision of the relevant services. Fees should be nondiscriminatory and proportionate

Market Abuse Regulation

MAR in a nutshell

What is MAR?

- Regulation (EU) No 596/2014 of the European Parliament and of the Council of April 16, 2014 on market abuse (market abuse regulation) and repealing Directive 2003/6/EC of the European Parliament and of the Council and Commission Directives 2003/124/EC, 2003/125/EC and 2004/72/EC
- EU law setting out uniform rules applicable throughout the EU aimed against types of unlawful behavior in financial markets, notably insider dealing, unlawful disclosure of inside information and market manipulation ("market abuse"), and providing for specific and prescriptive rules of conduct for issuers incorporated in the European Union, their management and other market participants

1 Insider dealing

In a nutshell

Prohibition to trade in financial instruments when in possession of "inside information", with prohibition to deal in company's financial instruments imposed on management during "closed periods"

2 Disclosure obligations

In a nutshell

Obligation on issuers to immediately publicly disclose "inside information" when it arises, with ability to defer disclosure if certain conditions are met

3 Unlawful disclosure

In a nutshell

Obligation to keep inside information confidential, unless disclosure is made in the normal course of an employment, a profession or duties (and safe harbor for "market soundings")

All three obligations/prohibitions based on the core concept of "inside information"

See next slides for definition

4 Market manipulation

In a nutshell

MAR prohibits certain manipulative or misleading market behavior, *e.g.*:

- Entering into transactions, placing orders or conducting behavior likely to give misleading signals as to supply, demand or price of a financial instrument
- Orders, transactions or behaviors which are likely to secure a price for a financial instrument at an artificial level
- Spreading false or misleading information as to supply, demand or price of a financial instrument

Lists of prohibited conduct and acceptable market practices exist

The core concept – Inside information

Precise	Price sensitive
Not public	Relates to issuers or financial instru-ments

— According to article 7(2) MAR, information is deemed of a precise nature "*if it indicates a set of circumstances which exists or which may reasonably be expected to come into existence, or an event which has occurred or which may reasonably be expected to occur, where it is specific enough to enable a conclusion to be drawn as to the possible effect of that set of circumstances or event on the prices of the financial instruments* […]" (emphasis added)

— Two sub-criteria:

- "**Reality**" criterion:
  - European Court of Justice of June 28, 2012, *Geltl v. Daimler*: "[…] *in using the terms 'may reasonably be expected', [MAR] refers to future circumstances or events from which it appears, on the basis of an overall assessment of the factors existing at the relevant time, that there is a realistic prospect that they will come into existence or occur. The question whether the required probability of occurrence of a set of circumstances or an event may vary depending on the magnitude of their effect on the prices of the financial instruments concerned must be answered in the negative.*" (emphasis added)
  - In "protracted" processes (such as M&A negotiations): each intermediate step as well as the future end result (or even a future intermediate step) may be "precise" enough, and could qualify as inside information
- "**Inference**" criterion:
  - European Court of Justice of March 11, 2015, *Lafonta v. AMF*: "[…] *it need not be possible to infer from that information, with a sufficient degree of probability, that, once it is made public, its potential effect on the prices of the financial instruments concerned will be in a particular direction*" (emphasis added)
  - Since *Lafonta*, criterion understood to basically only exclude vague information

The core concept – Inside information (*cont'd*)

Precise	**Price sensitive**
Not public	Relates to issuers or financial instru-ments

- According to article 7(4) MAR, information is deemed of a price sensitive nature "*if it were made public, would be likely to have a significant effect on the prices of financial instruments, […] shall mean information a reasonable investor would be likely to use as part of the basis of his or her investment decisions*" (emphasis added)
- Essentially a "reasonable investor" test
- Link with inference test of the "precise" limb of the definition: "price sensitivity" limb effectively operates as a *de minimis* filter by excluding information that would have no or minimal impact on price

Precise	Price sensitive
Not public	**Relates to issuers or financial instru-ments**

- Both criteria typically straightforward to assess except in specific situations (such as listings of various financial instruments in a cascade of entities)
- Public nature of the information depends on past (intentional) issuer communication and other publicly available information
- Relation to financial instruments or their issuers to be construed broadly, an indirect relationship suffices

Insider dealing and unlawful disclosure

1

Article 14 (a) and (b) MAR prohibits insider dealing, as well as attempts and inducements of insider dealing

Insider dealing?	For whom?	Exceptions?
— Acquiring or disposing of a financial instrument to which the inside information relates — For own account or account of third party — Includes cancelling or amending an earlier order — Requires "use" of inside information (but presumption of use applies in case the person is in possession of inside information) — Recommending or inducing another person to use inside information is also covered (*i.e.*, "tipping")	— Members of the corporate bodies of the issuer, shareholders, employees and external advisors who possess inside information — Persons involved in criminal activities who possess inside information — … *and* anyone who possesses inside information *if* such person knows or ought to know that the information constitutes inside information — Therefore universally applicable, also to non-EU investors/activists	— MAR contains lists of presumed "legitimate behaviors", but their use for illegitimate purposes may still be considered insider dealing — Use of inside information obtained in the conduct of a public takeover or merger and used solely for the purposes of proceeding with that merger or public takeover can be legitimate — The mere fact that a person uses its own knowledge that it has decided to acquire or dispose of financial instruments in the acquisition or disposal of those financial instruments is not necessarily, in itself, insider dealing *(cf.* Recitals 28 and 31)

2

Article 14 (c) MAR prohibits unlawful disclosure of inside information

Unlawful disclosure?	For whom?	Exceptions?
— Any dissemination of inside information to any person	— Same persons as insider dealing above	— Disclosure made "*in the normal exercise of an employment, a profession or duties*" — Ensure recipient is bound by confidentiality — Safe harbor for "market soundings"

MAR decision tree – Issuer perspective

Issuer perspective

Information relating to an issuer of shares traded on an EU regulated market

Is it inside information?

→ **No**

Yes

Choice between:

Or

Immediate public disclosure (by way of a press release)

Defer disclosure

DEFERRAL CONDITIONS

1. Legitimate interests
2. Not likely to mislead public
3. Ensure confidentiality (incl. NDA)

\+ *Ex post* notification to FSMA

\+ Obligation to maintain insider lists

LEAKS AND RUMORS

- Obligation to disclose kicks in also in the case of rumors (including from external sources), if sufficiently accurate to indicate confidentiality has been breached

Insiders prohibited from dealing

Including no access to capital markets for issuer

No (selective) disclosure

Except within normal course of professional duties and confidentiality is ensured

Activist situation

Activist approach ? ?

Negotiating settlement ? ?

"Insider tainting" ? ?

MAR decision tree – Activist perspective

For the activist

Information relating to an issuer of shares traded on an EU regulated market

Is it inside information?

No

Yes

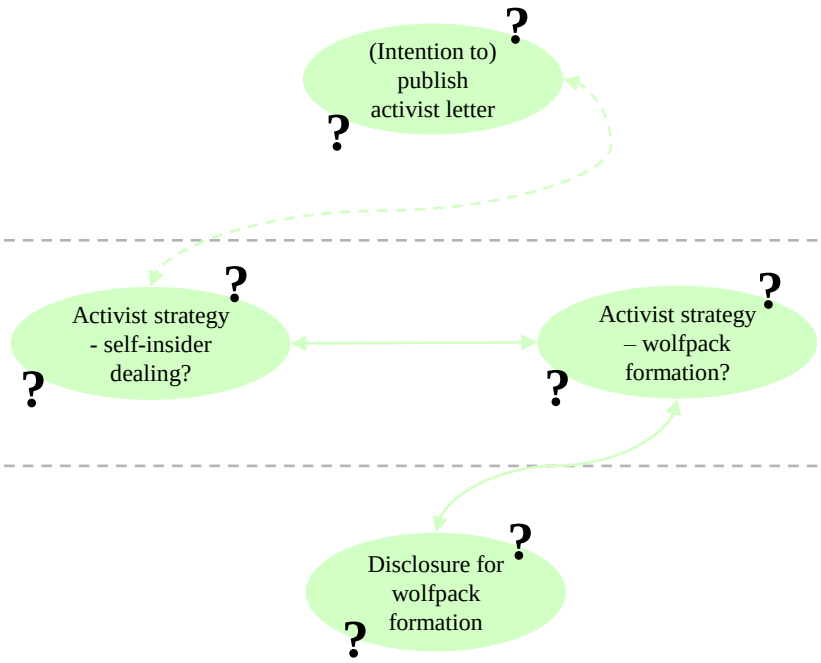
Insiders prohibited from dealing

"Own knowledge" exception available (cf. recital 31) + "own research" (cf. recital 28)?

No disclosure

Except "within normal course of professional duties"

Activist situation



Market manipulation

1. MARKET MANIPULATION

— Important risk and means of pressure for both the activist shareholder and the target, BUT…

- ➢ Often difficult to prove "false or misleading signals" as to the evaluation of a financial instrument or secures the price of a financial instrument "at an abnormal or artificial level"
- ➢ Increasing use of anonymous or pseudonymous accounts on digital media platforms

— "Political" activism

2. ALTERNATIVES?

— **Investment recommendations** (MAR)

- ➢ Requirement of reasonable care to ensure that information is objectively presented, and disclosure of interests or indication of conflicts of interest regarding the financial instruments to which the information relates

— **Defamation** (outside MAR)

- ➢ Legal considerations: burden of proof
- ➢ Practical considerations: could lead to (public) investigation into plaintiff company itself

Acting in concert

Acting in concert

Focus of presentation

1 **Transparency Law**

In a nutshell

Persons that are "acting in concert" for purposes of the Transparency Law are required to notify the FSMA and the issuer when crossing the relevant threshold

2 **Takeover Bid Rules**

In a nutshell

Persons that are "acting in concert" for purposes of the Takeover Bid Rules may be required to make a mandatory offer when crossing the 30% threshold

3 **Company Code**

In a nutshell

Persons that are "acting in concert" for purposes of the CCA cannot participate in a vote on limitation or cancellation of preemptive rights when holding more than 10%

All three obligations/prohibitions based on the core concept of "acting in concert"

See next slides for definition

4 **Joint control**

In a nutshell

A form of "control" that drives the "group" notion and related consequences under Belgian law

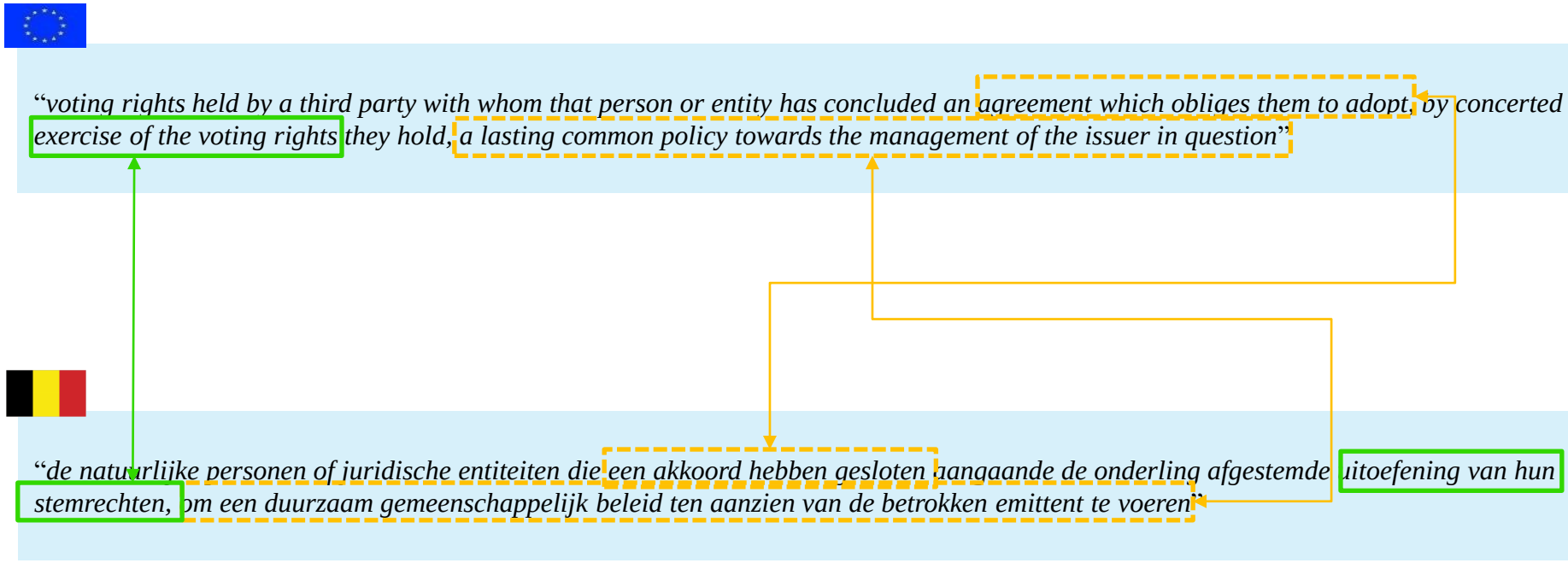
— Parent vs. subsidiary

— Independent party vs. related party

→ Consolidation circle, related party transactions, rules on financial support etc.

Related but different concept

The two legs of acting in concert – Transparency Law



- Legislator has been mixing up concepts: the definition meant for use in the Takeover Bid Rules (*see* next slide) has been imported in the Transparency Law too
- Former leg (c) ("*de natuurlijk of rechtspersonen die een akkoord hebben gesloten aangaande het bezit, de verwerving of de overdracht van stmrechtverlenende effecten*") was repealed by the law of June 27, 2016

The two legs of acting in concert – Takeover Bid Rules

"*natural and legal persons who cooperate with the offeror or the offeree company on the basis of an agreement, either express or tacit, either oral or written, aimed either at acquiring control of the offeree company or at frustrating the successful outcome of a bid*"

"*de natuurlijke personen of rechtspersonen die met de bieder, met de doelvennootschap of met andere personen samenwerken op grond van een uitdrukkelijk of stilzwijgend, mondeling of schriftelijk akkoord dat ertoe strekt de controle over de doelvennootschap te verkrijgen, het welslagen van een bod te dwarsbomen dan wel de controle over de doelvennootschap te handhaven*"

- Legislator has been mixing up concepts: the definition meant for use in the Transparency Law (*see* previous slide) has been imported in the Takeover Bid Rules too

The two legs of acting in concert – Takeover Bid Rules (*cont'd*)

ESMA public statement: information on shareholder cooperation and acting in concert under the Takeover Bids Directive

?

— "White list" of activities in which shareholders may engage and which engagement will not, in and of itself, lead to those shareholders being regarded as persons acting in concert

  - *E.g.*, entering into discussions with each other about possible matters to be raised with the company's board, table draft resolutions for items included or to be included on the agenda of a general meeting, call a general meeting other than the annual general meeting *etc*.

— Not a true safe harbor as each engagement needs to be determined on its own particular facts and that the national competent authorities may take into account "all other relevant factors" in making their decisions

— Does not cover the appointment of board members, which is an action on which shareholders will want to typically cooperate

— The regulators can sidestep the statement as it is not legally binding on them, thus creating significant uncertainty

Takeover Bid Rules - Triggers

Acting in concert

- Look at the voting securities held by persons acting in concert (in addition to those held by their "related persons" *etc.*)
- No possibility to "opt out" for part of shares from the acting in concert assessment (<> Transparency Law)

+

Crossing of threshold

- 30% threshold can be crossed by the concert parties in the aggregate or by an individual party to the concert action

+

Due to an acquisition

- One of the concert parties acquires voting securities within 3 years after the acting in concert commenced

OR

- One of the concert parties transfers its shares to a third party, who accedes to the concerted action (unless the parties to the original concert action always maintained a shareholding of more than 30%)

=

MTO obligation

- In case the 30% threshold is being crossed by the concert parties in the aggregate, they each have the obligation to launch a takeover bid
- In case the 30% threshold is being crossed by one of the concert parties, the obligation to launch a takeover bid only exists for the party that crossed the 30% threshold and not for its fellow concert parties

!

The mere entry into of a shareholder pact / creation of wolfpack will not lead to the MTO obligation being triggered → an essential feature of the MTO regime is that the 30% threshold should crossed due to **an acquisition**, *i.e.*, the mere entry into of a shareholder agreement should not trigger the requirement

…but is it worth the risk?